Book Reviews

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Helpman, E.: *The Mystery of Economic Growth.* 240 pp. Harvard University Press, 2004. Hardcover, £16.95

When one of the great scholars in the field outlines his views on economic growth, it deserves our attention and raises expectations. Elhanan Helpman's book undoubtedly fulfils these expectations. It provides a broad picture and insightful discussions about the determinants of economic development.

The discussion is entirely informal, but this is its strength rather than its weakness. It thereby allows policy makers and academics alike to obtain a view on the factors which cause growth. It is useful even for specialists in the field of growth to sharpen own conclusions from the vast literature surrounding this fascinating topic. In particular, the clear subjective evaluations expressed by the author, derived from a richness of evidence and theoretical arguments in the book, is complementary to standard textbooks.

The book starts with some plain facts, on the disparity of GDP per capita across countries, the distribution of growth rates, and economic development. It then proceeds by discussing the relative importance of different factors contributing to growth – factor accumulation versus productivity growth. This discussion also presents the different routes which growth theory has taken since Solow's famous neoclassical growth model. Professor Helpman convincingly explains why neoclassical growth theory, even when augmented by human capital, cannot account for the bulk of variation in countries' growth rates. Particularly, it cannot deal with the apparent divergence in per capita income across countries. This suggests a critical role of productivity growth, which not only differs across countries, unlike assumed in neoclassical growth theory, but itself triggers accumulation, thereby overstating the relative importance of accumulation in standard growth accounting.

Modern growth theory has proposed two approaches to endogenize total factor productivity (TFP) growth: first, by externalities from accumulation (e.g., learning-spillovers across workers), and second, by endogenous technical change driven by R&D investments of firms. The author points out that he believes that externalities are important, but at the same time stresses that a definite answer on the magnitude of these effects has not been reached yet.

Clearly, R&D-based TFP growth is at the heart of the author's view on growth. One theme emerging from this focus is the presence of international knowledge spillovers and the effects of trade. The review in chap. 5 suggests that both domestic and foreign R&D capital stocks have substantial effects on a country's TFP growth, and the effect of foreign R&D activity is greatly enhanced by goods trade. The author concludes that developing countries substantially benefit from R&D in industrial countries, while at the same time R&D is a source of divergence between North and South (as the effect of domestic R&D is especially large on domestic TFP growth of the richest countries). That trade is beneficial should not be taken for granted. If trade liberalization induces developing countries to specialize in primary goods, it may crowd out sectors which exhibit increasing returns to scale and learning-by-doing effects. Although stressing the evidence on positive effects of trade on growth in the aftermath of World War II, the author carefully points out that trade effects may be contingent on a country's characteristics like its comparative advantages in production. For instance, during the globalization wave in the 19th century, plenty of evidence suggests that, on average, a free trade regime (low tariffs) were in fact harmful for growth. Ironically, this occurred at a time when the second industrial revolution took place, and the book leaves this coincidence of historical development as subject for future research.

The final two chapters of the book are reserved for the most recent developments in the field of growth: the relationship between inequality and growth and the role of politics and institutions for growth. In chap. 6, Professor Helpman expresses the view that, by and large, income inequality tends to slow down growth and that the channels for this are poorly understood. These conclusions may be debatable. First, there is not much evidence on any clear relationship of income inequality and growth in developed countries (if anything, it seems to be positive). Second, my own reading of the available evidence (not only cross-country but also recent micro-evidence) is that it clearly supports the hypothesis that credit-market imperfections (e.g., borrowing constraints to finance education) significantly contribute to a negative impact of higher inequality on growth in developing countries. With respect to the other direction of the inequality-growth relationship, the author convincingly argues that recent (and in some countries dramatic) increases in earnings inequality across the globe are strongly related to (so-called "skill-biased") technological change. In contrast, market integration (the alternative suspect for the apparent shifts in income distribution) seems to have considerably less impact. The chapter ends with some good news. Although there is increasing divergence between countries, by and large, poverty in developing countries clearly declines over time.

The issue on political institutions and development is the one where the author expects most progress in the near future. The key motivation for this literature is that many factors which are highly correlated with growth – capital investment, education and R&D – are all endogenous in the sense that incentives to undertake these activities depend on rules and the organization of a society, like the legal system, property rights, public support for education, or the trade regime. Naturally, as chap. 7 reviews a much dispersed and fast growing field, it is the most incoherent part of the book. It starts with a discussion on the historical link between the evolution of property rights protection and organizational change in the production process. It then turns to evidence which suggests that countries with common-law system have less harmful regulations and lower levels of corruption than countries with a French civil-law system. Finally, the author takes up the controversy about the relative importance of geographical and institutional factors for growth and reviews political economy approaches. The author views political economy issues – like the role of special interest groups for economic development or the transition from autocracy to democratic institutions – as fruitful topics for future research. On the former issue, he clearly takes the viewpoint that geography matters, but only through its effect on institutions. This hypothesis is supported by two sets of historical evidence. First, as argued by Acemoglu, Johnson and Robinson in a series of papers, there is evidence that in regions with high settler mortality, European colonizers have set up "extracting states", while introducing property rights legislation in regions which have been more favorable to settlement. Second, evidence by Engerman and Sokoloff for the Americas suggests that the abundance but very unequal distribution of natural resources and fertile land in the southern colonies have led to political and economic institutions which were not conducive to growth. This points to a salient role of the apparent bias of political power towards plantation owners for understanding the failure of these economies to keep up with industrialization in many other parts of the world. Professor Helpman does not attempt to provide an explanation about the exact links, as this is subject to ongoing research. But he could have mentioned that Engerman and Sokoloff themselves point to the role of the apparent failure of these economies to support mass education by providing an effective public education system.

This brings me to some final remarks on this "tale of growth economics" (as the book is referred to in the preface). The book is strikingly cautious with respect to policy implications, and especially makes no clear statement regarding education policy. The reader may be left with the impression that this is related to the prominent role of R&D for growth stressed in earlier parts of the book. However, the bulk of R&D spending in industrialized countries is on wage costs for researchers. Moreover, a skilled labor force is also critical for successful adoption of technology in less developed countries. Hence, the question arises how to promote R&D, as one may target public spending either to pay firms R&D subsidies or to support education of scientists, engineers and users of new technology. Another question which emerges from the emphasis on R&D in the book is how competition policy and the patent system should be designed. For instance, conventional wisdom suggests that monopoly rents provide incentives to innovate. However, as Aghion and co-authors have argued, higher competition may induce technologically advanced firms to escape competition by innovating. It would have been interesting to come to know the author's viewpoint on these much debated policy issues. Nevertheless, the range of topics covered in the book is impressive. The tale of growth economics is told not only skillfully but also is – despite the complexity of the issues involved – very accessible. And for researchers in the field of growth, it is an invitation to look for the relevant issues and tackle the mystery of economic growth that remains.

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Duménil, G., and Lévy D.: Capital Resurgent: Roots of the Neoliberal Revolution. VI, 249 pp. Harvard University Press, Cambridge, Mass. 2004. Hardcover £35.95.

Unconventional interpretations of the globalization process can be refreshing in times when many economists, at least in Europe, feel somehow uncomfortable with the conventional views of the evolution of the world economic system. One of the merits of this book lies in its clear and unusual way of presenting and interpreting a large amount of macroeconomic data. Another merit is its ability to look at them not just with an economic eye, but also from a historical and social perspective: it raises a number of questions that may attract the curiosity of political scientists, policy makers concerned with the problem of inequality as well as economists dissatisfied with conventional modelling approaches.